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ABSTRACT

This brief report summarizes a longer document with the same title. It reviews the need to better manage higher education expenses in light of budget cuts and reductions in appropriations and other public services. It is noted that tuition, although increasing, has been increasing at a slower rate since 1981. Also, faculty salaries have not increased sufficiently to compensate for losses attributed to inflation, administration costs have risen as much as two percentage points over the past decade, greater pressures have been brought to bear on institutions to fund student aid, and endowment earnings are at their lowest in a decade. Institutions of higher education caught in the revenue/cost squeeze now have a variety of cost control management options open to them, some of which have already been adopted. The diversity, although great, suggests some common themes as part of a cost management strategy. These include specifying the mission of the institution; setting priorities among the programs and building a data base of trends and projections about revenues and costs; and applying break-even analysis to determine which programs are financially self-supporting, which are breaking even, and which require subsidies. Contains 7 references. (GLR)

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Strategies and Consequences: Managing the Costs in Higher Education

by John S. Waggaman

The need for better management of higher education's resources is a theme of great urgency as 40 states plan or actually cut appropriations to higher education and other public services. The 1987 hearings in Congress about higher education costs and the several reports which have appeared in the past 30 months provide data and information about cost trends, tuition increases, and explanations for the changes.

The breadth of this topic has required a wide-ranging survey of the professional literature covering several decades, for many of these problems have been encountered before, for example, the late 1960s. The topic cuts across many aspects of higher education: general revenues, the relationship of costs to tuition increases, faculty salaries and work load, research expenses, administrative costs, and other related subjects. Management actions, practices, and strategies in both private and public colleges and universities are discussed; the short- and long-range responses to financial emergencies are described.

The persistent theme is that analysis, planning, budgeting, and managing can prepare us for an uncertain financial future. We can avoid many of the more damaging pitfalls if we know the secondary consequences of the more typical ad hoc decisions made when financial difficulties arrive.

What Are the Rising Costs and Changing Revenues?

Although tuition continues to increase, it has been rising at a decreasing rate of growth since its peak in 1981 (Frances 1990). Rising costs are partly responsible for tuition increases as well as spending pressures and revenue shortfalls, according to Frances. Uncontrollable costs come from the marketplace and government mandates; spending pressures emerge from salary and fringe-benefit costs.

It still is true that faculty salaries have not increased sufficiently to compensate for the losses during the runaway inflation of the 1970s (Hauptman 1990). The 1990-1992 recession promises to make this problem worse. The anticipation of the enrollment decline in the number of high school graduates in the 1990s has led private institutions to spend funds to make campuses more attractive, add programs, and carry out full-fledged marketing campaigns for new students. Administrative costs have risen as much as two percentage points over the past decade, but the causes are not clear. The rise could be attributed to more student services and programs to meet governmental social policy and health and safety requirements, and the expanding use of computers in all kinds of administrative functions (Chaney and Farris 1990). The 1990 Chaney and Farris survey of financial officers indicated a majority thought that the addition of computers and the upgrading of computer facilities (72 percent) were very important causes in the 1980s. Rising insurance costs were selected by 71 percent of the officers as a major cost pressure.

Revenue shortfalls occur in two ways: a relative decline in the rate of growth so that inflation or other factors rise faster than revenues or an actual decrease in funding occurs. Endowment earnings for 1989-90 were at their lowest in a decade. By early 1992, it appeared that 22 states had cut 1992 appropriations to higher education; more are expected. The unwillingness of Congress to fully fund student aid up to the amounts it had authorized or to keep aid level with inflation makes it harder for students to obtain adequate funding at even low-cost public institutions.

However, the federal government still funds or underwrites almost three-fourths of student aid awarded in the United States. Unfortunately, that rate is down from 83 percent in 1980-81. These declines have caused public institutions and many private ones to spend more of their unrestricted general funds for student aid—as much as 25 percent of total aid in many institutions—up from 12 percent in 1980-81 (Frances 1990).

Institutions have been making very serious commitments in support of their special responsibility to recognize talent and help it enroll in college. Institutional aid also may help recruit students to offset some of the decline in the number of high school graduates. However, funds used for one purpose (or not collected) cannot be used to enhance programs or the salaries of faculty and staff. These latter needs might translate into pressures to raise tuition further so that more funds can be obtained for educational programs or other special purposes. A conceptual explanation of the dynamics of rising costs and revenues can be found in "The Lattice and the Ratchet" and other articles published in *Policy Perspectives* (June 1990 and later) of the Pew Higher Education Research Program.\

How Can We Manage and Control Costs?

The Chaney and Farris survey revealed that financial officers (81 percent) were quite confident about being able to control expenditures. If anyone should doubt that possibility, they should recall the finding from Cheit's follow-up study in 1973. He revisited the institutions he identified in 1971 that were in financial difficulty and

found they had cut annual expenditure growth from 4.0 percent to 0.5 percent, a reduction called "phenomenal" by Clark Kerr.

Today, after several potential management "revolutions" (Keller 1983; Rourke and Brooks 1966), colleges and universities have a variety of management tools available to help control costs, *once the leaders and administrators have decided to do so*. Some institutions successfully have adopted various information, analysis, and accountability methods to improve their planning and management abilities (Baldridge and Tierney 1979). However, there is no single strategy for successfully managing costs. Furthermore, the management revolutions might have been only partially successful, although the current fiscal crisis should stimulate increased interest in these tools and techniques.

There are some common themes in the reports about what could or should be part of a cost management strategy. First is to clarify the mission of the institution, then set priorities among the programs (educational, service, administrative, student, etc.). Strategic planning with a clear focus on both the external environment and internal operations is necessary to build a data base of trends and projections about revenues and costs. Break-even analyses for the various programs need to be calculated to determine which programs are financially self-supporting, those that break even, and those that require subsidies. Data from the break-even analyses, along with a thorough program review, should reveal the areas from which funds could be obtained for enhancements and new programs. Many other activities need to be considered—such as those that revolve around administrative compliance procedures—so that funding requests and accountability reports are accepted at face value. These strategies should be in place before the next financial emergency arrives. Otherwise, it's back to short-term ad hoc solutions, some undesirable secondary consequences, and then a search for better solutions, with such processes spiraling on into the future. One can't help wondering if there isn't a better way.

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